INDEX

	Page
Opinions below	2
Jurisdiction	2
Question presented	2
Statute involved	2
Statement	3
Argument	5
Conclusion	11

CITATIONS

Cases:

Caplin v. *Marine Midland Grace Trust Co.*, 406 U.S. 416	1
Case v. *Los Angeles Lumber Products Co.*, 308 U.S. 106	7
Country Life Apartments v. *Buckley*, 145 F.2d 935	7
Granville & Winthrop Bldg. Corp., In re, 87 F.2d 101, certiorari denied *sub nom. Keig* v. *Lloyd*, 301 U.S. 702	9
Gross v. *Bush Terminal Co.*, 105 F.2d 930	9
Murel Holding Corp., In re, 75 F.2d 941	9
Protective Committee v. *Anderson*, 390 U.S. 414	1
Regional Rail Reorganization Act Cases, Nos. 74-165 to 74-168, decided December 16, 1974	6
Texas Hotel Securities Corp. v. *Waco Development Co.*, 87 F.2d 395, certiorari denied *sub nom. Waco Development Co.* v. *Rupe*, 300 U.S. 679	8

Statutes and rule: Page

Bankruptcy Act, Chapter X, as added, 52 Stat. 883, *et seq.*, 11 U.S.C. 501, *et seq.*:

Sec. 174, 11 U.S.C. 574 3
Sec. 175, 11 U.S.C. 575 4
Sec. 179, 11 U.S.C. 579 ..... 2, 4, 5, 6
Sec. 208, 11 U.S.C. 608 1
Sec. 216, 11 U.S.C. 616 5
Sec. 216(1), 11 U.S.C. 616(1) 5
Sec. 216(7), 11 U.S.C. 616(7) 6, 7, 8
Sec. 216(7)(b), 11 U.S.C. 616(7)(b) 7
Sec. 216(8), 11 U.S.C. 616(8) 2, 4, 5, 6, 7, 8, 10
Sec. 236, 11 U.S.C. 636 7

Rule 21(4), Rules of the Supreme Court of the United States 1

Miscellaneous:

6 Collier, *Bankruptcy* (14th ed., 1972 rev.) 7

In the Supreme Court of the United States

OCTOBER TERM, 1974

No. 74-1112

JAMES H. PRICE, PETITIONER

v.

STACEY W. COTTON, TRUSTEE

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FIFTH CIRCUIT

BRIEF FOR THE SECURITIES AND EXCHANGE COMMISSION IN OPPOSITION [1]

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[1] The Securities and Exchange Commission has been participating in this reorganization proceeding in the district court as a party pursuant to Section 208 of Chapter X of the Bankruptcy Act, as added, 11 U.S.C. 608, since shortly after the proceeding commenced in 1971. It has taken positions in that court and in the court of appeals similar to the positions urged herein. As in *Protective Committee* v. *Anderson*, 390 U.S. 414, 420 n. 3, and *Caplin* v. *Marine Midland Grace Trust Co.*, 406 U.S. 416, 419 n. 8, the Commission is "an unnamed respondent before this Court." See Rule 21 (4) of the Rules of this Court.

OPINIONS BELOW

The order of the court of appeals affirming *per curiam* the order of confirmation of the district court (Pet. App. A-1) is reported at 505 F. 2d 732. The order of the district court (Pet. App. A-3) and the report of the bankruptcy judge sitting as special master (Pet. App. A-11) are unreported.

JURISDICTION

The judgment of the court of appeals (Pet. App. A-2) was entered on December 6, 1974. The petition for a writ of certiorari was filed on March 6, 1975. The jurisdiction of this Court is invoked under 28 U.S.C. 1254(1).

QUESTION PRESENTED

Whether a plan of corporate reorganization under Chapter X of the Bankruptcy Act may be confirmed, although rejected by the debtor's shareholders, when the plan provides that the shareholders may choose to receive cash in excess of the value of their shares as found by the court.

STATUTE INVOLVED

The provisions of Chapter X of the Bankruptcy Act that are relevant to the question presented are Sections 179 and 216(8), as added, 55 Stat. 892 and 896, 11 U.S.C. 579 and 616(8). These provisions are set forth at Pet. App. A-59 and A-66.

STATEMENT

Atlanta International Raceway, Inc. ("debtor") filed a voluntary petition for reorganization under Chapter X of the Bankruptcy Act on January 18, 1971. The debtor had outstanding an eight percent mortgage note of $1,000,000 plus accrued interest, other debt in the aggregate amount of $426,521, and 320,254 shares of common stock held by over a thousand persons (App. 6-7).[2]

After a hearing, the debtor was found to be solvent with a reorganization value for its stock of about $1.00 per share. A proposed reorganization plan was found to be "fair, equitable and feasible" (Pet. App. A-14) and was approved, pursuant to Section 174 of the Act, 11 U.S.C. 574. The plan provided that the mortgage debt would be partially paid off and the remainder would be assumed, at a nine percent interest rate, by the reorganized debtor. Junior lien creditors would have the option of receiving a new junior note or new shares of the reorganized debtor's stock. Unsecured creditors would receive new shares in satisfaction of their claims. New shares would also be issued for cash to the sponsors of the plan. The existing stockholders were to retain their shares, which would represent approximately 18 to 26 percent of the shares outstanding upon completion of the reorganization.

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[2] "App." refers to the joint appendix filed in the United States Court of Appeals for the Fifth Circuit.

The plan was then submitted to creditors and stockholders, pursuant to Section 175 of the Act, 11 U.S.C. 575. The several classes of creditors accepted the plan, but the stockholders rejected it. The sponsors of the plan thereupon filed a proposal for the protection of dissenting stockholders, pursuant to Sections 179 and 216(8) of the Act, whereby all shareholders who chose to do so would receive $1.60 in cash for their shares from the sponsors (Pet. App. A-42).

The district judge confirmed the plan as amended, adopting the report of the bankruptcy judge, finding that it "provides more than 'adequate protection' pursuant to Section 216(8)" for the dissenting stockholders (Pet. App. A-42) and that the plan with "the adequate protection provided for the dissenting shareholder class [3] is fair, equitable and feasible and that it should be * * * confirm[ed]" (Pet. App. A-9, A-11, A-44).

Petitioner, a shareholder who acquired his shares after the Chapter X proceedings had begun, and who was a co-sponsor of a competing plan, appealed. He did not challenge the adequacy of the $1.60 per share option given to the shareholders, but contended solely that the stockholder protection provisions of Section 216(8) of Chapter X are inapplicable where a debtor has only one class of stockholders and a majority of that class rejects the plan. The court of appeals affirmed without opinion (Pet. App. A-1).

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[3] Confirmation was subject to a provision that any stockholder could also purchase shares at $1.60 up to an amount equal to that already held by him (Pet. App. A-42).

ARGUMENT

The decision below is in accord with established principles and does not present any issue warranting review by this Court.

Chapter X of the Bankruptcy Act is designed to provide court-supervised relief for financially troubled corporations. The primary goal of a Chapter X proceeding is to afford an opportunity for rehabilitation rather than liquidation by preserving the going-concern value of the debtor while allowing an opportunity for development of a plan for reorganization of the debtor's financial structure.

Section 216 of the Act sets forth both mandatory and optional provisions regarding reorganization plans. Section 216(1) provides that a plan "may include in respect to stockholders generally or some class of them, provisions altering or modifying their rights, either through the issuance of new securities of any character or otherwise." If a plan is found to conform to the requirements of the Act, it is then submitted to creditors and, if the debtor is solvent, to stockholders, for approval. See Section 179 of the Act.

If the stockholders reject the plan, Section 216(8) of the Act provides that a plan "shall provide for any class of stockholders which is affected by the plan and does not accept the plan by the majority of the stock required under this chapter, adequate protection for the realization by them of the value of their equity, if any, in the property of the debtor dealt with

by the plan, either as provided in the plan or in the order confirming the plan, * * * (b) by appraisal and payment in cash of the value of their stock * * *." [4]

Petitioner's sole contention in this Court, as in the courts below, is that Section 216(8) does not apply where a debtor has only one class of stockholders and a majority of that class rejects the plan. This contention is contrary to both the purpose and statutory scheme of Chapter X of the Act.

There are apparently no reported decisions specifically holding that Section 216(8) can be utilized when a majority of the single class of shareholders fails to accept a plan. The reason probably is that it has always been assumed that Section 216(8) can be so utilized. The correctness of this conclusion is shown by other provisions of Chapter X relating to confirmation of plans, and by case law construing these provisions with respect to dissenting creditors.

Although Section 179 requires acceptance of a plan by two-thirds of each class of creditors and, if the debtor is solvent, by a majority of each class of stockholders, that section excludes from the required majorities, creditors or stockholders "* * * for whom payment or protection has been provided as pre-

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[4] A comparable provision relating to creditors not accepting the plan appears in Section 216(7) of the Act. Such provisions, which are designed to avoid frustration of reorganizations while providing protection for dissenting shareholders or creditors, are often referred to as "cram-down" provisions and are a common feature of reorganization statutes. See the *Regional Rail Reorganization Act Cases*, Nos. 74-165 to 74-168, decided December 16, 1974, slip op. 47.

scribed in paragraphs (7) and (8) of section 216 of the Act * * *." Thus, the section of Chapter X that confers voting rights on creditors and/or stockholders makes clear that voting rights may effectively be withdrawn if a creditor or shareholder is afforded adequate protection for his financial interest in the debtor under the cram-down provisions of Sections 216(7) and (8). Section 179 thus shows that the cram-down provisions of Sections 216(7) and (8) can be used to surmount the objections of dissenting creditors and shareholders.[6] See 6 Collier, *Bankruptcy* ¶ 7.35, pp. 1295-1296 (14th ed., 1972 rev.).

This conclusion is supported by *Country Life Apartments* v. *Buckley*, 145 F.2d 935 (C.A. 2), where confirmation of a plan was upheld even though neither of two affected classes of creditors accepted the plan. That case involved Section 216(7)(b), which provides that creditors are adequately protected by "* * * a sale of * * * [the debtor's] property free of * * *

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[6] Petitioner's contention (Pet. 5-7) that Section 236 of Chapter X, 11 U.S.C. 636, requires the judge either to dismiss the proceeding or to adjudicate the debtor a bankrupt where no plan is accepted would effectively nullify Sections 179 and 216(7) and (8). Section 236 is primarily concerned with the situation where a plan is either unnecessary, in which case dismissal should occur, or impossible due to the gravity of the debtor's financial situation, in which case liquidation under ordinary bankruptcy provisions can be directed. This Court has held that failure to accept a plan, standing alone, does not compel dismissal and that the district court may permit a reasonable time for a new proposal to be offered where it appears that a fair and equitable plan may be adopted. *Case* v. *Los Angeles Lumber Products Co.*, 308 U.S. 106, 131-132.

claims, at not less than a fair upset price * * *." The court rejected the argument that the creditors' assent was nonetheless required for confirmation of the plan (*id.* at 938):

> Appellants further urge that the plan should not have been confirmed, since it lacked the assent of a two-thirds majority of any class of creditors. * * * Under Bankruptcy Act, § 179, no acceptance need be obtained from a class of creditors or stockholders "for whom payment or protection has been provided as prescribed in" § 216(7, 8). See 3 Gerdes on Corporate Reorganizations, 1936, § 1113. The trustee's plan contained a provision for the sale of the property at not less than the $525,000 upset price, which, as we have seen, was the accepted fair value of the property, and for a transfer of the nonassenting creditors' claims to the proceeds. Since the nonassenting creditors were thus adequately protected under the trustee's plan, their assent did not constitute a necessary prerequisite to confirmation.

Compare *Texas Hotel Securities Corp.* v. *Waco Development Co.*, 87 F.2d 395, 400 (C.A. 5), certiorari denied *sub nom. Waco Development Co.* v. *Rupe*, 300 U.S. 679, where the court of appeals, in discussing what constituted adequate protection for dissenting creditors under the subsection of former Section 77B of the Bankruptcy Act (the predecessor of Chapter X) which was substantially identical to Section 216(7) of Chapter X, stated: "Payment of the face of the claim in cash is the perfect realiza-

tion of a money chose in action." Accord, *Gross* v. *Bush Terminal Co.*, 105 F.2d 930, 932 (C.A. 2).

These decisions demonstrate that if creditors are afforded adequate protection by the cram-down provisions, their consent is not necessary to the confirmation of a reorganization plan. This principle is equally applicable to shareholders.

Petitioner's reliance (Pet. 7) on *In re Granville & Winthrop Bldg. Corp.*, 87 F.2d 101 (C.A. 7), certiorari denied *sub nom. Keig* v. *Lloyd*, 301 U.S. 702, is misplaced. That case involved a cram-down provision that permitted the district court to employ "such method as will, under and consistent with the circumstances of the particular case equitably and fairly provide * * * protection" for dissenting creditors. The quotation from the court's opinion that suggests that this general provision does not permit confirmation over the objections of creditors must be read in light of the court's finding that the plan did not in fact provide adequate protection (87 F.2d at 103). The decision merely reflects the principle that cram-down provisions must provide "indubitable equivalence" to dissenting creditors. *E.g.*, *In re Murel Holding Corp.*, 75 F.2d 941, 942 (C.A. 2). The cash payment in this case, which gives the nonassenting shareholders substantially more than the value of their shares, manifestly satisfies the requirement.*

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* Petitioner has never, and does not now, challenge the finding that $1.60 per share provides adequate protection for the shareholders. No such challenge could be made in

Contrary to petitioner's contention (Pet. 7, 8), the cram-down provisions of Section 216(8) do not render superfluous the confirmation provisions of the Act concerning acceptances and voting eligibility. Rejection of the plan may result in dismissal of the Chapter X proceedings or liquidation in ordinary bankruptcy, if there are no sponsors with sufficient resources to afford adequate protection to dissenters. But where adequate protection is provided by the plan (and particularly where, as here, the protection is in the form of a cash payment in excess of the value of the shares), the efficacy of Chapter X proceedings would be seriously impaired if dissenters could nonetheless prevent the rehabilitation of the debtor. Petitioner offers no convincing reason why the principle should not apply where there is only one class of shareholders.

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light of the finding, also not challenged, that the fair value of the shares is at most $1.00. See Pet. App. A-38 to A-39.

CONCLUSION

For the foregoing reasons, it is respectfully submitted that the petition for a writ of certiorari should be denied.

ROBERT H. BORK,
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LAWRENCE E. NERHEIM,
General Counsel,
Securities and Exchange Commission.

APRIL 1975.

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